IN THE

United States Court of Appeals

FOR THE NINTH CIRCUIT

PHOENIX TITLE &
TRUST COMPANY,
Appellant,

vs.

MYLES STEWART, Trustee of the
Estate of ARTHUR PEABODY and
OLIVE PEABODY,
Appellees.

No. 18819

ON APPEAL FROM THE UNITED STATES
DISTRICT COURT FOR THE
DISTRICT OF ARIZONA

REPLY BRIEF FOR APPELLANT PHOENIX TITLE & TRUST COMPANY

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STATEMENT ON THE FACTS OF THE CASE

Throughout all briefs in this case there has been a difference of opinion between the parties as to the facts. Appellee has stated as a fact the "intention of the parties" in the execution of Exhibits 2 (Deed), 3 (Trust Agreement), 4 (Note) and 5 (Collateral Assignment), but has cited no testimony on this point. Likewise, Apellee has contended the Peabodys were in "possession" to date of bankruptcy whereas Appellant has contended it was in possession at that time. It will serve no purpose to reallege the facts contended by Appellant, so Appellant realleges the facts stated in all its briefs filed in this action, together with its fact citations in support thereof.

ARGUMENT

I

AS RESPECTS APPELLEE'S POSITION IN RE INCHOATE LIEN

The authorities cited by Appellee Stewart on pages 13 and 14 of Appellee's answering brief have heretofore been discussed at length and distinguished on pages 22 to 25 of Phoenix Title's opening brief as Appellant Suffices it to say none of the cases cited by Appellee Stewart pinpoint any particular in which the lien of Phoenix Title & Trust fails for want of choateness. The doctrine of choateness of liens was re-explained last November in *Hammes v. Tucson Newspapers, Inc.*, 324 F.2d 101, when the Court of Appeals for the Ninth Circuit applied the doctrine to the lien of Tucson Newspaper arising out of its assignment of money payments to be received in futuro under a land contract.

At this point it might be well to distinguish between the Trustee in Bankruptcy attempting to determine priority between two competing liens, where one of the liens is a tax lien of the United States Government, and the situation where the Trustee in Bankruptcy is attempting to set aside a lien through the machinery of the Bankruptcy Act under §70(e). In the former situation, bankruptcy is really not involved. The trustee is simply a stakeholder trying to determine which of two competing lien holders is entitled to certain specific assets of the bankrupt. Such a situation is reflected in *Hammes v. Tucson Newspapers, Inc., supra*, where the bankrupty trustee was trying to determine if Tucson Newspapers was entitled to certain assets of the bankrupt, or the Federal Government under its recorded tax liens. In this latter situation where the Bankruptcy Act was not employed to set aside a lien, reference was made to

Federal law to determine the priority of the competing lien of Tucson Newspapers and in that particular case it will be noted that the court found that the recorded assignment of the payments to be received in futuro under the land contract constituted a choate and valid security device and that Tucson Newspapers was a "mortgagee" within the meaning of 26 USC §6323(a). The court also applied the same doctrine in *Hoare v. U.S.*, 9th Cir. 1961, where the situation involved competing liens, and again the security device employed there was determined to be a mortgage within the protection of §6323(a).

Such is not the situation in the instant case. Here the United States Government is not asserting its lien and the bankruptcy trustee is not acting as a stakeholder trying to determine which of two competing lienors is entitled to bankrupt assets. Instead, here the bankruptcy trustee is trying to subrogate himself under §70(e) of the Bankruptcy Act not to establish a priority of one lien over another, but rather to dissolve entirely or set aside the lien of Phoenix Title & Trust Company through §70(e). As previously stated in Phoenix Title & Trust Company's brief as Appellee, page 6, et seq., the doctrine of choateness of lien has been consistently rejected with other sections of the Bankruptcy Act where it was attempted to interpolate that doctrine arising under the Federal Tax Statutes into the machinery of the Bankruptcy Act itself. In any event, assuming that the doctrine of choateness of lien did apply to the operation of the Bankruptcy Act itself, it is clear that under all the tests the lien of Phoenix Title & Trust Company is choate as determined by the District Court in its order March 29, 1963 (TR 171) wherein it reversed the Referee on Conclusions of Law 11 and 13.

In addition, Appellee Stewart in asserting the doc-

trine of choateness of lien inconsistently jumps from federal law to state law in determining whether or not Phoenix Title & Trust Company's trust device is a mortgage. As this court held in *Hammes v. Tucson Newspapers, Inc.*, 324 F.2d 101 (9 Cir.) at page 103:

> "It also held that Tucson Newspapers is a mortgagee within the meaning of 26 U.S.C. §6323(a) which is a federal law question. Again we agree."

This court also held in *Hoare v. U.S.*, 294 F.2d 823 (9 Cir.) at page 825:

> "What is meant by the word 'mortgagee' as used in §6323(a) however is a federal question as to which state law is to be considered but is not controlling."

It is apparent from the foregoing that the doctrine of choateness of lien simply referable to Federal tax liens is not applicable to a case where the machinery of the Bankruptcy Act is being used in an atempt to dissolve an existing lien of a creditor. Where the Bankruptcy Act machinery is being used to set aside a lien, the only question is whether or not the lien of the creditor is valid under state law. The doctrine of choateness of lien applies in bankruptcy situations not where the Bankruptcy Act is involved, but simply where the trustee is a stakeholder attempting to determine between competing liens (one of which is a federal tax lien), which is prior under a situation which does not exist in the instant case.

It is also notable that in *Hammes v. Tucson Newspapers, Inc., supra,* the court found the assignment from Arizona Stores, Inc. to Tucson Newspapers, Inc. of payments to be made in futuro under a land contract constituted a mortgage device within the meaning of §6323(a), showing the wide scope of devices which the court has consistently found, so long as they were for security purposes, to constitute a mortgage within

the contemplation of §6323(a) of the Internal Revenue Code.

Nowhere has Appellee Stewart cited any authority for the proposition that the machinery of the Bankruptcy Act may be invoked by the bankruptcy trustee to clothe the trustee with special powers which apply to a sovereign government as is the situation with the Federal Government and the doctrine of choateness of lien as applicable to federal tax liens. On the other hand, Appellant Phoenix Title & Trust Company has cited two cases directly in point supporting the proposition that §70(e) of the Bankruptcy Act may not be used by a bankruptcy trustee to clothe the bankruptcy trustee with powers which are referable to a sovereign government. These are *Silverman v. Wedge*, 158 N.E. 2d 668, and *In the Matter of F. A. Whitney Carriage Company*, 173 F. Supp. 709. Those cases flatly hold that the bankruptcy trustee may not be subrogated to the special powers referable to a state government. It, therefore, follows that the same principle should apply to the proposition that the bankruptcy trustee may not be subrogated through §70(e) of the Bankruptcy Act to the special powers of the Federal Government.

II

ARGUMENT CONCERNING APPELLEE STEWART'S COMMENTS ON BARRINGER v. LILLEY

Appellee Stewart sets forth on pages 18 and 19 of his answering brief distinctions which he believes exist between *Barringer v. Lilley*, 96 F.2d 607, 9th Cir., from the instant case. The only difference (which is not material) is that in the instant case there were four instruments instead of three. In *Barringer v. Lilley* the court construed the three instruments there involved as

collectively constituting the security device. In the instant case it is Appellant Phoenix Title & Trust Company's position the court should in like manner construe collectively not three but four instruments as constituting the security device. The only significant difference between the two cases is that there exists a Trust Agreement (Exhibit 3) in the instant case, the purpose of which was to provide a vehicle by which sales could be made of lots to provide for funding the payment of the Promissory Note (Exhibit 4) secured by the Collateral Assignment (Exhibit 5). It scarcely seems logical that the existence of one instrument—a trust agreement providing for lot sales as a funding device for payment of the mortgage—should constitute a destruction of the mortgage itself; yet that apparently is the position of Appellee Stewart. The equivalent instruments in the two cases are simply the Declaration of Trust in Barringer which recited the $85,000.00 note and the Collateral Assignment (Exhibit 5) in the instant case, which does the same thing. Certainly, the addition of an additional security device—the Trust Agreement (Exhibit 3) which provides a funding device for payment of the mortgage —should not impair the security. The mere addition of this additional instrument appears to be the sole basis by which Appellee Stewart argues that the doctrine of *Barringer v. Lilley* is inapplicable to the instant case.

III

ARGUMENT CONCERNING APPELLEE STEWART'S COMMENTS ON STATUTE OF USES

Appellee Stewart on pages 19 through 23 of his answering brief in making comments on the Statute of Uses completely ignores Part B of Appellant Phoenix Title's opening brief in which Appellant cites the neces-

sity to construe the instruments creating its lien together. Clearly, if the critical instruments involved in this appeal, the Trust Deed (Exhibit 2), the Trust Agreement (Exhibit 3), the Promissory Note (Exhibit 4) and the Collateral Assignment of Beneficial Interest (Exhibit 5) are construed together, those collective instruments create a security device equivalent to a mortgage and the application of the doctrine of the Statute of Uses is no more pertinent there than it would be with the statutory California trust deed. In any event, the duties of the trustee in enforcing the mortgage are such active duties as to bring the device beyond the purview of the Statute of Uses and it should be noted at this point that a primary basis of Phoenix Title's appeal in this case is the arbitrary refusal of the Referee, sustained by the District Court, to construe the above instruments together, notwithstanding the fact that they were executed and delivered concurrently on July 26, 1956, and not withstanding the legal authorities cited on page 12 of Appellant Phoenix Title's opening brief. Nowhere is there any evidence in the record nor has there been legal authority cited to sustain the Referee's refusal to regard these instruments collectively.

But assuming that the Referee in the District Court may be sustained in this arbitrary division of the instruments involved, first into trust instruments and then into security instruments, it is Appellant Phoenix Title's position that the Statute of Uses has not been executed, but under the cited authorities, including the Restatement of Trusts, Section 131, as cited by Appellee Stewart on page 20, the duties of Phoenix Title & Trust Company as Trustee were positive, affirmative duties at such time as lot sales were made to convey title to the real property sold to the respective purchasers; that these were mandatory duties so that the trust could not, even under this

strained construction of the collective instruments, be a passive trust.

Thus, the Trust Agreement (Exhibit 3) page 1 provides:

> ". . . that the Trustee holds and will hold the title to said property in trust for the purpose of subdividing, platting, deeding, selling, conveying, receiving payment for and otherwise handling the property as a whole or in lots or parcels, upon such terms and conditions and for such prices as the Trustee may be instructed in writing so to do by the Beneficiaries or their authorized representative . . ."

The fair import of the foregoing is that when notified of a lot sale the trustee was under a mandatory duty to convey the lot sold to the purchaser.

The Court is referred to the extensive argument of Appellant, Phoenix Title, in its opening brief, pages 15 to 24.

CONCLUSION

In view of the authorities, facts and arguments set forth above and in Appellant's opening brief, Appellant submits:

1. That the doctrine of choateness of lien as rejected by the District Court is not applicable in a bankruptcy situation except in the situation where the bankruptcy trustee is acting simply as a stakeholder and deciding between two or more competing liens, one of which is a federal tax lien.

2. That the facts of the instant case come within the doctrine of *Barringer v. Lilley, supra,* and that a distinction between that case and the instant case cannot, logically, be predicated solely on the proposition that there

was an extra instrument, to-wit, a trust agreement which simply provided a vehicle for funding the payment of the mortgage by lot sales.

3. That the Referee in District Court erred by failing to construe the critical instruments involved in this appeal together notwithstanding that all evidence showed that they were executed and delivered concurrently on July 26, 1956, and notwithstanding the fact that all existing legal authority provides, in the absence of evidence to the contrary, that the instruments should be construed collectively and together, and if the critical instruments involved in this appeal are construed together, the Statute of Uses simply is not applicable to a situation where the device employed as urged by Appellant, Phoenix Title & Trust Company, is simply a mortgage. On the other hand, if the instruments are not construed together, the affirmative duties of the trust agreement including the duty to convey when lot sales are made reflect an active trust so that the Statute of Uses is not executed. Finally, Appellant urges that the application of the Statute of Uses to terminate the trust should be confined to special situations such as where partition of trust assets is desirable in the case of long inactive trusts as reflected in the cases cited by the District Court and as discussed on page 23 of Appellant's opening brief.

Respectfully submitted,
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By.....
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I certify that, in connection with the preparation of this Brief, I have examined Rules 18 and 19 of the United States Court of Appeals for the Ninth Circuit and that, in my opinion, the foregoing Brief is in full compliance with those rules.

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